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C O N F I D E N T I A L SECTION 01 OF 03 ASUNCION 000733

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SUBJECT: EX-FINANCE MINISTER BORDA BRIEFS AMBASSADOR ON HIS
RESIGNATION AND FUTURE PLANS

REF: A) Asuncion 726

B) Asuncion 675

Classified By: Ambassador John F. Keane for reasons: 1.4(b)
and (d).

1. (C) Summary: The Ambassador hosted ex-Minister of Finance Dionisio Borda and his top advisor, Fernando Masi at a private breakfast on May 27. Borda claimed that he had been forced out under a pretext (see ref B) to clear the way for excessive, politically motivated economic stimulus in advance of May 2006 internal party elections. President Duarte's naming of former Minister of Industry and Commerce Ernst Bergen (ref A) to replace Borda, and the fact that Bergen kept nearly all of Borda's team at Finance, suggest that Borda's fears may be overblown. We will withhold judgment until the new economic team takes some concrete actions. End Summary.

2. (C) On May 27, ex-Minister of Finance Dionisio Borda and his chief advisor Fernando Masi, both of whom resigned on May 19, came to the Ambassador's residence for breakfast. Over more than two hours, Borda gave his views on his resignation, President Duarte, the economy and his future plans. Borda, a non-partisan technocrat, was an effective Finance Minister whose integrity was never questioned. Nevertheless, his views remain colored by his perception that he was forced out of the government and should be taken in that context.

BORDA SPEAKS OUT -- ONCE

3. (U) On May 22, a local paper published an interview with ex-Minister Borda, his only public comments since his resignation speech on May 19. In the interview, Borda characterized his resignation as the "story of a death foretold" and asserted that he was forced out for political reasons. He claimed that President Duarte was under enormous pressure to generate jobs and more rapid economic growth in advance of May 2006 internal party elections, and that he (Borda) had come to be seen as an obstacle. Borda warned that an artificial "bubble" would be unsustainable and would have familiar negative results.

4. (C) During the breakfast, Borda said he gave the interview with the goal of generating discussion about economic policy going forward. After the interview was published, new Minister of Finance Bergen reiterated publicly the GOP's commitment to fiscal responsibility, said he would resign before helping create an unsustainable bubble, and announced that the GOP would seek an IMF program, possibly one lasting through Duarte's term. (See Ref A for a readout of the Ambassador's initial call on Minister Bergen.)

5. (C) Borda considered those developments public pledges of restraint and IMF engagement to be positive outcomes from his resignation. He also stated that his interview with ABC would be his last comments to the press, as he did not want to become a destabilizing force. Borda expressed confidence in Bergen, characterized him as a friend, and said he had offered his advice and counsel. He also said that Bergen had told him that he would resign before giving in to pressures to artificially inflate the economy.

VIEWS ON IMF AND THE ECONOMY

6. (C) Borda believes that an IMF program provides the Executive branch with a powerful tool to resist political pressures and helps provide an important forward-looking reform plan. He recalled relating to President Duarte that during a visit to Taiwan, after giving a presentation on Paraguay's advantages for investors, the first question he was asked was how much longer the IMF program ran. He told

the Ambassador that he favored seeking a three-year Extended Fund Facility (EFF) for its longer term and focus on structural reform, rather than another Stand-by Arrangement (SBA). He described his meetings with the Fund in Tokyo and later in Washington at the Spring Meetings as productive. He had used the "Plan for Economic Growth with Equity" developed by Borda's team in consultation with the private sector as a basis for a program and claimed that it was well received by both Anoop Singh and Takatoshi Kato.

17. (C) Both Borda and Masi agreed that any attempt to artificially inflate the economy would be doomed to fail, and eventually ruin the progress made so far. Borda said he had told President Duarte that Peru's Alan Garcia provided an instructive example of the perils of economic manipulation. Instead, Paraguay's economy requires real reform to bolster confidence and attract investment. For Borda, the five most important areas requiring reform are: the labor code, the public banks, state-owned enterprises, the social security agency (IPS), and the civil service law.

18. (C) The Ambassador asked Borda how he thought one might go about reactivating the economy, even temporarily. Borda had to think for a minute, reflecting the dearth of options (outside of monetary emission). He suggested that funds to stimulate the economy could come from the binational entities that run the Itaipu and Yacyreta dams, from the Social Security Fund, and possibly directly from the Treasury (which he said has cash reserves of about 800 billion guaranies, or about US\$128 million in times greater than when he arrived at the Ministry).

VIEWS ON DUARTE FRUTOS AND HIS OWN DEPARTURE

19. (C) Borda repeated his claim that Paraguay is entering a political cycle in advance of May 2006 internal party elections, and that he had been forced out to pave the way for the creation of an economic "bubble". He claimed that there was tremendous pressure from the Congress and other ministries to increase spending. He also speculated that President Duarte was increasingly concerned by some polls that have shown his approval rating falling while his disapproval rating has climbed.

110. (C) He described at length the chain of events leading to his resignation. He believes that there were several contributing factors, including the increasing effectiveness of three units he had created: the UCIP public investment monitoring unit, a "Results Based Management" unit set up to track the results of budget expenditures of other ministries, and a public enterprises unit. He also cited efforts to send home up to 200 tax inspectors not currently being utilized due to concerns of past malfeasance. (These workers would still be paid, as current civil service rules make it nearly impossible to fire them, but they would be physically relocated so as not to obstruct the work of the other tax administration employees.)

111. (C) Borda stated that he was forced out by the President's insistence that he sign a decree acknowledging a Ministry of Finance debt to the Central Bank that had been previously extinguished by a decree of former President Gonzalez Macchi. In Borda's view and that of his legal counsel, signing the decree would have subjected him to significant legal risk, and he was obligated to refuse and resign. He had argued that the dispute should be settled by the courts, where it has since been directed, which Borda takes as confirmation that his ouster was planned.

112. (C) Borda and Masi provided some examples of the GOP's impatience, including a strong push by the Minister of Public Works to obtain \$300 million in loans from Brazil for public works that are tied to the significant use of Brazilian contractors, carry high interest rates, and would be administered by a trust outside the purview of the Ministry of Finance. This despite what Borda and Masi claimed was over \$200 million in loans from the Japanese Bank for International Development (JBIC) on tap with an interest rate of 2.5% and a 30-year term, but which is contingent on the passage of an acceptable public banking law. They also mentioned the possibility of \$40 million in grants from Mercosur for infrastructure spending, but suggested that the timing (at least a year away) was too slow for those interested in immediate results.

FUTURE PLANS

113. (C) Borda and Masi are both partners in a think tank and consultancy called CADEP. They noted that it had been mostly dormant while they had been occupied at the Ministry of Finance, and that they would now turn their attention to reviving the organization, which is their livelihood. Borda asked the Ambassador for support, perhaps with CADEP conferences in the future.

COMMENT

¶14. (C) Ex-Minister Borda remains proud based on his long list of extraordinary accomplishments. His relationship with President Duarte was strained for much of his tenure, with at least four prior occasions (only one of which became public) of Borda's near resignation. Borda also had a reputation within the Ministry of Finance as being inflexible in his prescriptions.

¶15. (C) Borda's warning of the possible creation of an economic bubble does not entirely square with other personnel moves made by President Duarte of late. As noted in ref A, Bergen is a strong, honest and apolitical Minister who may strike a more collaborative stance with the private sector than Borda did, but who is unlikely to follow party orders to unleash a wave of unsustainable economic stimulus. As Bergen pointed out, he kept most of Borda's team intact, including the Vice Minister in charge of the tax department.

¶16. (C) Borda did a tremendous job in helping achieve macroeconomic stability, clear Paraguay's arrears, and jumpstart the structural reform process. It is too early to judge until we see more concrete actions from Minister Bergen and Monica Perez, the new President of the Central Bank who is coming from her job as an IMF staff economist to assume the post, but at this juncture, Borda's warnings may reflect a strong desire to see his good start continued, and perhaps even some sour grapes. The sky is not yet falling in Paraguay.

KEANE#